

TREO MAINTENANCE ASSOCIATION

DATE: August 2022
TO: Treo Maintenance Association
FROM: Rina Sagal, Community Manager

Dear Homeowner:

In accordance with California Civil Code Section 5305 this notice is to advise you that the Annual Audit for the fiscal year end December 31, 2021 has been completed. This audit was prepared by an independent CPA firm, Owens, Moskowitz and Associates, Inc. and has been accepted by the Board of Directors. You may view a copy of the complete audit at www.myhoa.com/treo.

Please be advised, as a property owner, you have the right under California Civil Code Section 4950 to obtain copies of minutes of the Board of Directors meetings for a nominal fee. You may send your request in writing to the Board of Directors in care of Management at the address below.

The meetings of the Board of Directors are scheduled to be held on a regular basis on the third Tuesday of the odd months via zoom. These meeting dates are subject to change or cancellation if there is a lack of quorum of the Board. Please call StoneKastle Community Management to confirm the meeting you plan to attend.

Should you have any questions, regarding the enclosed information, please contact the Board, in writing or attend a Board meeting.

TREO MAINTENANCE ASSOCIATION

Audited Financial Statements

For The Year Ended December 31, 2021

TABLE OF CONTENTS

	PAGE
INDEPENDENT AUDITORS' REPORT	3-4
BALANCE SHEET	5
STATEMENT OF REVENUE, EXPENSES AND ASSOCIATION FUNDS	6
STATEMENT OF CASH FLOWS	7
NOTES TO FINANCIAL STATEMENTS	8-11
SUPPLEMENTAL INFORMATION	12
SUPPLEMENTAL INFORMATION ON FUTURE MAJOR REPAIRS	13

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Treo Maintenance Association

Opinion

We have audited the accompanying financial statements of Treo Maintenance Association (a California corporation), which comprise the balance sheet as of December 31, 2021, and the related statements of revenue, expenses and association funds, and cash flows for the year then ended, and the related notes to the financial statements.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Treo Maintenance Association as of December 31, 2021, and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of Treo Maintenance Association and to meet our other ethical responsibilities in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about Treo Maintenance Association's ability to continue as a going concern within one year after the date that the financial statements are available to be issued.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with generally accepted auditing standards will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with generally accepted auditing standards, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of Treo Maintenance Association's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about Treo Maintenance Association's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control related matters that we identified during the audit.

Report on Supplementary Information

Accounting principles generally accepted in the United States of America require that the information on future major repairs and replacements of common property on page 13 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Financial Accounting Standards Board, which considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Owens, Moskowitz and Associates, Inc.

Owens, Moskowitz and Associates, Inc.

July 11, 2022

TREC MAINTENANCE ASSOCIATION
BALANCE SHEET
DECEMBER 31, 2021

	OPERATING FUND	REPLACEMENT FUND	TOTAL
ASSETS			
Cash	\$ 51,066	\$ 505,558	\$ 556,624
Short-Term Investments	-	800,000	800,000
Assessments Receivable	26,060	-	26,060
Less: Allowance For Doubtful Accounts	(9,825)	-	(9,825)
Interest Receivable	-	172	172
Prepaid Taxes	3,431	-	3,431
Prepaid Insurance	7,185	-	7,185
Prepaid Expenses	5,701	-	5,701
	<u>\$ 83,618</u>	<u>\$ 1,305,730</u>	<u>\$ 1,389,348</u>
Total Assets	<u>\$ 83,618</u>	<u>\$ 1,305,730</u>	<u>\$ 1,389,348</u>

LIABILITIES AND ASSOCIATION FUNDS

Liabilities			
Accounts Payable	\$ 3,882	\$ -	\$ 3,882
Prepaid Assessments	21,113	-	21,113
Deferred Assessments (Assessments Received In Advance - Replacement Fund)	-	1,305,730	1,305,730
	<u>24,995</u>	<u>1,305,730</u>	<u>1,330,725</u>
Total Liabilities	<u>24,995</u>	<u>1,305,730</u>	<u>1,330,725</u>
Commitments			
	-	-	-
Association Funds	<u>58,623</u>	<u>-</u>	<u>58,623</u>
Total Liabilities And Association Funds	<u>\$ 83,618</u>	<u>\$ 1,305,730</u>	<u>\$ 1,389,348</u>

SEE INDEPENDENT AUDITORS' REPORT AND ACCOMPANYING NOTES

TREO MAINTENANCE ASSOCIATION
STATEMENT OF REVENUE, EXPENSES AND ASSOCIATION FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2021

	OPERATING FUND	REPLACEMENT FUND	TOTAL
REVENUE			
Assessments	\$ 222,100	\$ 55,466	\$ 277,566
Price Adjustment - Bad Debt	(1,644)	-	(1,644)
Interest Income	3	761	764
Other Income	9,548	-	9,548
Total Revenue	230,007	56,227	286,234
EXPENSES			
Landscape Maintenance	87,767	-	87,767
Management Fees	18,635	-	18,635
Administrative	8,816	-	8,816
Legal And Audit	1,678	-	1,678
Insurance	28,655	-	28,655
Pest Control	3,168	-	3,168
General Maintenance	22,790	890	23,680
Reserve Study	450	-	450
Electricity	7,459	-	7,459
Water	12,516	-	12,516
Street Repair	-	6,122	6,122
Doors	-	41,406	41,406
Fence	-	7,813	7,813
Lighting and Electrical	206	-	206
Income Tax	6	-	6
Total Expenses	192,146	56,231	248,377
Excess (Deficiency) of Revenue Over Expenses	37,861	(4)	37,857
Association Funds Balance Beginning of Year	20,766	-	20,766
Interfund Transfers	(4)	4	-
Association Funds Balance End of Year	\$ 58,623	\$ -	\$ 58,623

SEE INDEPENDENT AUDITORS' REPORT AND ACCOMPANYING NOTES

TREC MAINTENANCE ASSOCIATION
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2021

	OPERATING FUND	REPLACEMENT FUND	TOTAL
Cash Flows From Operating Activities:			
Cash Received From Members	\$ 223,765	\$ 150,500	\$ 374,265
Cash Paid To Suppliers of Goods And Services	(197,652)	(56,231)	(253,883)
Interest Received	3	981	984
Net Cash Provided By Operating Activities	26,116	95,250	121,366
Cash Flows From Investing Activities:			
Purchase of Short-Term Investments	-	(150,000)	(150,000)
Cash Flows From Financing Activities:			
Interfund Transfers	(4)	4	-
Interfund Borrowings	(25,000)	25,000	-
Net Cash Provided By (Used In) Financing Activities	(25,004)	25,004	-
Net Increase (Decrease) In Cash And Cash Equivalents	1,112	(29,746)	(28,634)
Cash And Cash Equivalents At Beginning of Year	49,954	535,304	585,258
Cash And Cash Equivalents At End of Year	\$ 51,066	\$ 505,558	\$ 556,624

RECONCILIATION OF EXCESS OF REVENUE OVER EXPENSES
TO NET CASH PROVIDED BY OPERATING ACTIVITIES

Excess (Deficiency) of Revenue Over Expenses	\$ 37,861	\$ (4)	\$ 37,857
Adjustments To Reconcile Excess (Deficiency) of Revenue Over Expenses To Net Cash Provided By Operating Activities:			
Change In Assessments Receivable	(11,584)	-	(11,584)
Change In Interest Receivable	-	220	220
Change In Prepaid Insurance	(665)	-	(665)
Change In Prepaid Expenses	(5,701)	-	(5,701)
Change In Prepaid Taxes	6	-	6
Change In Accounts Payable	854	-	854
Change In Deferred Assessments	-	95,034	95,034
Change In Prepaid Assessments	5,345	-	5,345
Net Cash Provided By Operating Activities	\$ 26,116	\$ 95,250	\$ 121,366

SEE INDEPENDENT AUDITORS' REPORT AND ACCOMPANYING NOTES

TREG MAINTENANCE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2021

NOTE 1 NATURE OF ORGANIZATION

Treo Maintenance Association was incorporated on January 13, 2005, in the state of California. It is responsible for the operation and maintenance of the common property within the development, which is located in the city of Irvine, California. The development consists of 135 residential units.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Method of Accounting

The books of Treo Maintenance Association are maintained on the modified cash basis of accounting with entries made to convert them to the accrual basis for audit and tax purposes.

Fund Accounting

The Association's governing documents provide certain guidelines for governing its financial activities. To ensure observance of limitations and restrictions on the use of financial resources, the Association maintains its accounts using fund accounting. Financial resources are classified for accounting and reporting purposes in the following funds established according to their nature and purpose:

- Operating fund - This fund is used to account for financial resources available for the general operations of the Association.
- Replacement fund - This fund is used to accumulate financial resources designated for future major repairs and replacements.

Deferred Assessments (Assessments received in advance-replacement fund)

The Association recognizes revenue from members as the related performance obligations are satisfied. Deferred assessments (assessments received in advance-replacement fund) are recorded when the Association has the right to receive payment in advance of the satisfaction of performance obligations related to replacement reserve assessments. The activity in deferred assessments (assessments received in advance-replacement fund) during 2021 was as follows:

Deferred Assessments, at January 1, 2021	\$ 1,210,696
Assessments Budgeted for Replacement Reserve	150,500
Revenue Released to Match Reserve Expenses	<u>(55,466)</u>
Deferred Assessments, at December 31, 2021	\$ <u>1,305,730</u>

Cash Equivalents and Short-term Investments

Cash equivalents consist primarily of certificates of deposit and other securities with original maturities of 90 days or less. Certificates of deposit and other securities with original maturities over 90 days are classified as short-term investments. Cash equivalents and short-term investments are stated at cost, which approximates market value.

SEE INDEPENDENT AUDITORS' REPORT

TREC MAINTENANCE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2021
(CONTINUED)

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Member Assessments

Association members are subject to monthly assessments to provide funds for the Association's operating expenses and major repairs and replacements. Assessment revenue is recognized as the related performance obligations are satisfied at transaction amounts expected to be collected. The Association's performance obligations related to its operating assessments is satisfied over time on a daily pro-rata basis using the input method. The performance obligations related to the replacement fund assessments are satisfied when these funds are expended for their designated purpose. Assessments receivable at the balance sheet date are stated at the amounts expected to be collected from outstanding assessments from unit owners. The Association's policy is to retain legal counsel and place liens on the properties of homeowners whose assessments are thirty days or more delinquent. Any excess assessments at year end are retained by the Association for use in the succeeding year. At December 31, 2021, the Association had delinquent assessments of \$9,825, where an allowance for uncollectible accounts is deemed necessary.

The Association treats uncollectible assessments as variable consideration. Methods, inputs, and assumptions used to evaluate whether an estimate of variable consideration is constrained include consideration of past experience and susceptibility to factors outside the Association's control. Assessments receivable as of the beginning and end of the year were \$13,538 and \$26,060, respectively.

Property and Equipment

Real property and common areas acquired by the original homeowners from the developer are owned by the individual owners in common and are not capitalized on the Association's financial statements.

Replacements and improvements to the real property and common areas also belong to the owners and are not capitalized on the Association's financial statements.

Credit Losses

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326)*. This guidance represents a significant change in the accounting model for credit losses by requiring immediate recognition of management's estimates of "current expected credit losses". Under the prior model, losses were recognized only as they were incurred, which FASB has noted delayed recognition of expected losses that might not yet have met the threshold of being probable. The new model is applicable to all financial instruments that are not accounted for at fair value through net income, thereby bringing consistency in accounting treatment across different types of financial instruments and requiring consideration of a broader range of variables when forming loss estimates. Although this change affects any entity holding financial instruments (ie: trade receivables or investments in debt securities) the financial services industry by its nature bears the most exposure. The effect of adoption of this standard will be to accelerate the recognition of credit losses. The effective date of this standard is for years beginning after December 15, 2023, with early adoption allowed. We do not plan an early adoption of this standard.

Use of Estimates

The Association uses estimates and assumptions in preparing these financial statements in accordance with generally accepted accounting principles. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. Actual results could vary from the estimates that were used.

SEE INDEPENDENT AUDITORS' REPORT

TREC MAINTENANCE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2021
(CONTINUED)

NOTE 3 FUTURE MAJOR REPAIRS AND REPLACEMENTS

The Association's governing documents require funds to be accumulated for future major repairs and replacements. Accumulated funds are held in separate accounts and are generally not available for operating purposes. It is the Association's policy to allocate interest earned on such funds to the replacement fund. Since the actual costs are dependent upon the frequency of occurrence and future costs, there is no assurance that this fund is adequate.

A study of the Association's funding program for the replacement of Association common areas, projected to December 31, 2021, indicates the Association's ideal cash replacement fund balance was \$ 1,179,611 at that date. The Association's total replacement fund total assets was 111% funded at December 31, 2021. The study recommends a 2022 contribution to the replacement fund of \$ 153,500 (\$ 94.75 per owner per month). The 2022 budgeted contribution is \$ 153,504.

The preparation of such a study involves significant estimates by the persons preparing the study, and these estimates are subject to annual revision for changing prices, circumstances and assumptions. If actual replacement costs exceed funds available, or where replacement of common areas is necessary where no fund has been previously established, the Association has the right to increase the monthly assessments, pass special assessments, or delay replacement until funds are available.

NOTE 4 INCOME TAXES

The Association is a corporation that is potentially taxable on all of its net income, including unspent member assessments. However, under state and federal filing elections, the Association may choose to be taxed only on its net non-membership income, which includes interest income.

The State of California allows qualifying homeowner associations to file an election to be taxed under special rules. Under this election, income from members (such as assessments) is exempt from taxation.

Federal law offers a similar election, which must be made annually. However, net non-membership income under this election is taxed at a flat rate of 30%. If the Association chooses to file as a regular corporation, it may still exclude from taxation its net membership income by making certain elections. Tax at the regular corporate tax rate is generally lower. Some of these elections, however, have come under IRS attack and certain issues are yet to be clarified. In 2021, the Association filed as an exempt association.

Regardless of how the Association files its taxes, non-membership income (interest) may not be offset with membership expenses (such as common area maintenance costs). That is why the Association's taxable income can be greater than its net income as recorded in the financial statements.

Accounting principles generally accepted in the United States of America require management to evaluate tax positions taken by the Association and recognize a tax liability if the Association has taken an uncertain position that more likely than not would not be sustained upon examination by the IRS. Management has analyzed the tax positions taken by the Association and has concluded that as of December 31, 2021, there are no uncertain positions taken or expected to be taken that would require recognition of a liability or disclosure in the financial statements. The Association is subject to routine audits by taxing jurisdictions; however, there are currently no audits in progress. The Association's management believes it is no longer subject to income tax examinations for years prior to 2017.

Federal and California income taxes have been accrued based on the taxable portion of the income reported in the accompanying financial statements.

SEE INDEPENDENT AUDITORS' REPORT

TREC MAINTENANCE ASSOCIATION
 NOTES TO FINANCIAL STATEMENTS
 FOR THE YEAR ENDED DECEMBER 31, 2021
 (CONTINUED)

NOTE 4 INCOME TAXES (Continued)

Income taxes for the current year were:

2021 INCOME TAXES	FEDERAL	STATE TAX	STATE FEE	TOTAL
Income Taxes	\$ -	\$ 6	\$ -	\$ 6
Less: Credit from prior year return	(2,680)	(757)	-	(3,437)
Prepaid tax	\$ 2,680	\$ 751	\$ -	\$ 3,431

NOTE 5 ASSESSMENTS

During 2021, assessments were billed at a rate of \$ 230 per unit per month. The rate is budgeted to remain at \$ 230 per unit per month for 2022.

NOTE 6 INTERFUND ACCOUNT

The interfund account represents the amount one fund owes another fund. Various scenarios may cause this situation which include, but are not limited to, one fund paying the expenses of another fund, one fund borrowing from another fund, or the operating fund not paying the full annual budgeted contribution amount to the replacement fund.

NOTE 7 CONTINGENCY

On March 11, 2020, the World Health Organization declared the novel strain of coronavirus (COVID-19) a global pandemic and recommended containment and mitigation measures worldwide. The outbreak in the United States has caused business disruption through mandated and voluntary closings of businesses and shelter in place orders. While the disruption is currently expected to be temporary, there is considerable uncertainty around the duration of the closings and shelter in place orders. It is at least reasonably possible that this matter will negatively impact the Association. However, the financial impact and duration cannot be reasonably estimated at this time.

NOTE 8 SUBSEQUENT EVENTS

The date to which events occurring after December 31, 2021, the date of the most recent balance sheet, have been evaluated for possible adjustment to the financial statements or disclosure is July 11, 2022, which is the date on which the financial statements were issued.

SEE INDEPENDENT AUDITORS' REPORT

SUPPLEMENTAL INFORMATION

TREC MAINTENANCE ASSOCIATION
 SUPPLEMENTAL INFORMATION ON FUTURE MAJOR REPAIRS
 AND REPLACEMENTS
 DECEMBER 31, 2021
 (UNAUDITED)

The board of directors contracted an independent consultant who conducted a August 2, 2021 study, projected to December 31, 2021 , to estimate the remaining useful lives and replacement costs of the components of common property. Funding requirements include an inflation factor of 2.5% and an interest rate of 1.5%.

The following table is based on the study and presents information about the components of common property.

Components	Estimated Remaining Useful Lives	Estimated Current Replacement Cost	2022 Funding Requirement	Recommended Fund Balances
Streets	0 to 12 years	\$ 117,931	\$ 7,396	\$ 72,159
Roofs - Tile Repairs	0 years	16,001	14,601	16,001
Painting	0 to 4 years	247,537	39,925	89,772
Gates/Railing/Walls	4 to 17 years	322,389	16,342	215,484
Lighting	9 to 12 years	137,775	5,978	80,585
Decks/Doors	4 to 24 years	602,213	36,495	351,628
Building Exterior	3 to 19 years	291,912	15,297	150,548
Grounds	7 to 12 years	45,400	2,662	22,075
Termite Control	2 years	165,375	10,334	147,000
Contingency	n/a	-	4,471	34,358
		<u>\$ 1,946,532</u>	<u>\$ 153,500</u>	<u>\$ 1,179,611</u>

As shown above, the study recommends a cash replacement balance of \$1,179,611 as of December 31, 2021 and contributions to reserves of \$153,500 during 2022. The Association's total replacement fund total assets at December 31, 2021 were \$1,305,558 or 110.68% of the recommended balance.

SEE INDEPENDENT AUDITORS' REPORT ON SUPPLEMENTAL INFORMATION